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Business for Sale? Get the Right Price

By Barbara Mannino - FOXBusiness

What's a business worth? Whatever someone is willing to pay for it. That's not just a cheap line, either.

There's no strict rule of thumb for pricing, because so many factors have influence, not the least of which is industry and type of business. But the nexus of pricing generally falls into three broad categories. Even so, remember that even similar businesses can often have wildly different valuations.

"A steak house has different multiples than Mexican or Chinese," said I. Alan Hirschfeld, a CPA, forensic accountant and principal-in-charge of Marcum LLP's Tinton Falls, N.J., office.

Earnings Valuation

There are two types of earnings, based on the size of the company. Businesses earning less than $1 million usually use a metric based on Seller's Discretionary Earnings, or SDE.

"You take net profit and add your salary back to it to show the prospective purchaser the profit of the business," said Bill Lange, a principal in the San Diego-based Vanguard Resources Group, a franchise of Vanguard Resources, a national business brokerage firm. "Your sale price is typically one to three times SDE."

Larger businesses, with earnings up to $30 million, typically base valuation on earnings before interest, taxes, depreciation and amortization, or EBITDA. In those cases, Lange said that selling price is typically three- to five-times EBITDA.

Past performance is only part of the equation. Make sure you're factoring in the future. "What do you think is going to happen in the future?

"'I have a great product or service with increasing demand and a solid client base,' you can say," said Hirschfeld. "'There's little risk and potentially unlimited growth.'"

On the other hand, “If you have one customer and you’re teetering on the brink of bankruptcy, you’re high risk,” Lange said.

Type of Buyer

The kind of buyer makes a difference, too. Broadly, they fall into three categories: investment equity ventures, insider groups and strategic buyers, said Chris Carey, principal of New York City-based Chris Carey Advisors.

An equity buy is low risk, because the seller is assured of getting paid. Often, this type of deal allows you to simply cash out and move on.

An insider group often poses the highest risk for a seller, since he is often part of the purchase. As the seller, you’ll usually have to hold a note, maybe even retain some other debt, Carey said.

A strategic buyer purchases because the business being sold includes complementary products and services. Here, your business is typically incorporated into a larger company.

Deal Structure

You can also structure deals to influence price. You might agree to stay on with the new buyers for awhile in a different capacity. As a result, you may take a lower selling price for a higher salary. A potential downside: You could discover that you are working in a different type of environment, said Carey. “Culture is sometimes lost, jobs are eliminated and the environment is often not as friendly,” he said.

Similarly, as a seller you don’t have to sell out at 100%. You can agree to stay on and consult and also sign a noncompete. Your willingness to do this as a seller can be worth something to the buyer and add extra dollars to your value.

Experts agree that a synergistic buy usually reaps the highest price. “Brand marriages—ones in which you get the right buyer and seller together—are made in heaven and can reap a fortune,” Hirschfeld said.